

MINUTES
REGULAR MEETING OF BOARD OF LAND COMMISSIONERS
November 19, 2007, at 9:00 a.m.
Room 303 State Capitol Building
Helena, Montana

PRESENT: Governor Brian Schweitzer, Attorney General Mike McGrath, State Auditor John Morrison, Secretary of State Brad Johnson, and Superintendent of Public Instruction Linda McCulloch

Mr. Morrison moved for approval of the minutes from the October 15, 2007, meeting of the Board of Land Commissioners. Seconded by Ms. McCulloch. Motion carried unanimously.

BUSINESS CONSIDERED:

1107-1 **FWP: SMITH RIVER – DEEP CREEK CONSERVATION EASEMENT**

Mary Sexton, DNRC Director, said the Deep Creek conservation easement is a donation made to FWP by the Mountain Lion, LLC, a corporation controlled by Dennis Washington, for 240 acres along the Smith River. The EA was completed and the FWP Commission has given final approval for the project. Tom Riley from FWP is here to answer any questions you may have.

Tom Riley, FWP Park Division Assistant Administrator, said before you today is the final approval for a 240-acre recreation and conservation easement along the Smith River in Cascade County. It is being donated by a private corporation and involves land that is owned by the Forest Service, FWP, and the BLM. It involves both sides of the Smith River and is where the mouth of Deep Creek hits the Smith River. It is a pristine area and a great coup for the floating public and recreationists of Montana. On behalf of FWP and the public, I'd like to thank Mr. McGrath for his encouragement and involvement over the past two years to reach the point we are at today. We had two public comments, both very positive.

Motion was made by Mr. McGrath to approve the Smith River-Deep Creek conservation easement. Seconded by Ms. McCulloch.

Mr. McGrath said that this is an extraordinary piece of real estate. It is great for the people of Montana, the Smith River, and the recreationists. I'd also like to formally express my gratitude to Dennis and Phyllis Washington as well as Senator Mike Halligan.

Governor Schweitzer said that 80 years ago the Anaconda Company purchased this property with the intention of putting dozers in there, tearing the mountain down, and pushing it into the Smith River because it contains a great deal of calcium bicarbonate and calcium carbonate. The mixture would then be slurried down the Smith River to the confluence of the Missouri and down to their smelter because it would be the least expensive way of getting carbonate for the smelter. I think this turned out to be a better use for that mountain than what was intended 80 years ago.

A vote was taken on the motion to approve. Motion carried unanimously.

1107-2 PRELIMINARY APPROVAL FOR MONTANA TECH LAND EXCHANGE
(BOARD OF REGENTS)

Ms. Sexton said the University of Montana, Montana Tech, is seeking preliminary approval for a proposed land exchange of small parcels within Butte in the Lawlor Addition. The Board of Regents previously approved this exchange and Montana Tech plans to hold a public comment hearing in Silver Bow County and return to the Land Board for final approval.

Cathy Swift, Office of the Commissioner of Higher Education, said Montana Tech is seeking to exchange small parcels of land for land that is much more usable for its purposes. The Board of Regents has reviewed this transaction and approved it as far as fair market value and it being in the best interest of the Montana University system, subject to approval from the Land Board. We do have an appraisal by a certified appraiser. We have not completed the environmental assessment process and we will have the public hearing before final approval by the Land Board.

Motion was made by Ms. McCulloch for preliminary approval of the land exchange. Seconded by Mr. McGrath. Motion carried unanimously.

1107-3 DMA: FINAL CONSIDERATION FOR THE ACQUISITION OF LAND FOR A
NATIONAL GUARD READINESS CENTER (MISSOULA ARMORY)

Ms. Sexton said this is a request for final approval of the acquisition of a National Guard Readiness Center, the Missoula Armory. It is a little over 30 acres. The purchase price is about \$2 million, which is less than the appraised value. This is nontrust land located in Missoula County. There is a representative here from the Department of Military Affairs to answer any questions.

Debra Lafontaine, Department of Military Affairs, said we are requesting approval for the purchase of 34.94 acres to construct a new armed forces reserve center. It is located adjacent to Highway 93 and I-90 in Missoula.

Motion was made by Mr. Johnson for final consideration of the land acquisition. Seconded by Mr. Morrison. Motion carried unanimously.

1107-4 QUIET TITLE ACTION – HOBSON-MOCCASIN-BENCHLAND

Ms. Sexton said we are seeking permission to file a quiet title to clarify title of three lots within Hobson-Moccasin-Benchland area. The state acquired these lots from a tax title from the estate of Johann and Fern Slenas. The conveyance from the estate was imperfect, and after clarifying the title to these lands the department will convey the requested lots to the high bidder who offered to purchase them. These parcels cannot be closed until the title is cleared.

Motion was made by Mr. McGrath for permission to file quiet title action. Seconded by Ms. McCulloch. Motion carried unanimously.

1107-5 QUIET TITLE ACTION – UPDEGRAFF V. STATE OF MONTANA

Ms. Sexton said this is for an irregularly shaped piece of land which is actually a portion of the lands described in the settlement because of an island that emerged from the Yellowstone River

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after statehood. The parties have agreed to settle the issue by delineating a line between the state island and private lands. Pursuant to this settlement agreement, title to the island will be held by the state in trust for the common schools.

Motion was made by Mr. McGrath for permission to file quiet title action. Seconded by Mr. Johnson. Motion carried unanimously.

Governor Schweitzer said can we do 1107-6 and 1107-7 together?

Ms. Sexton agreed.

1107-6 APPROVAL FOR COMMUNITIZATION AGREEMENT – DEVON ENERGY

1107-7 APPROVAL FOR COMMUNITIZATION AGREEMENT – HEADINGTON OIL

Ms. Sexton said 1107-6 is a request for approval of a communitization agreement with Devon Energy for a state tract of 40 acres within Choteau County. The department's tract comprises 6.25 percent of the communitized area. The department will receive 1.04 percent of gas production in this tract. The second tract (1107-7) is with Headington Oil Limited Partnership in Richland County and is a part of the Bakken formation. The state owns 320 acres out of a total of 1280 mineral acres. The state's tract is 25 percent of the area and the DNRC will receive 3.125 percent of all oil production. These two communitizations will allow the state to receive its proper share of production from these spacing units.

Motion was made by Ms. McCulloch to approve both the Devon Energy and Headington Oil communitization agreements. Seconded by Mr. Morrison. Motion carried unanimously.

1107-8 AVISTA CORPORATION SETTLEMENT – RIVERBED RENTAL

Ms. Sexton said this request is to approve the settlement for market value rental of the state's trust land riverbeds. The state of Montana and Avista Corporation have reached a settlement under the Montana Hydroelectric Resources Act in the matter of *PPL Montana et al. v. the State of Montana*. In the settlement, the parties have agreed that full market value for the annual rental rate for the 3100 acres in the Clark Fork riverbed is the amount of \$4 million annually. There will be an upward adjustment by the Consumer Price Index (CPI) beginning in calendar year 2008 and continuing to 2016. In 2016 the parties will confer and determine if the annual rate remains consistent.

David Hoffman, PPL Montana, said I have turned in written testimony which is fairly brief and I don't intend to re-read that. I would like to point out that PPL Montana does not take the position of approval on the Avista settlement, although we do urge the Board to examine the settlement on its terms only. The DNRC's description of the settlement, introducing this as an agenda item, is in part erroneous because the settlement does not adopt a shared net benefits calculation or methodology. Nor does the settlement hinge on generation power sales, cost of production, or any other element of benefits calculation. According to the notice on this agenda item, the only issue before the Board is the whether or not to approve the settlement. Therefore, the Board action applies only to Avista. The Board should not be adopting a policy for determining full market value for state lands underlying hydroelectric projects.

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Motion was made by Mr. McGrath to approve the Avista settlement. Seconded by Mr. Morrison.

Mr. McGrath said this is, as noted in the agenda item, a settlement. This was a hard-worked out discussion between the state's lawyers and the Avista attorneys. It was a settlement to avoid trial in this matter. Mr. Hoffman represents PPL. That case did indeed go to trial, and the decision on the issues raised by Mr. Hoffman is pending before Judge Honzel as we speak. This issue is different than that. This is a settlement, and with any settlement you compromise a number of issues. This is a very good settlement for the state of Montana. I think Avista would agree—there are a number of representatives here. It is a good settlement for Avista so we can move forward. I think this is a very good resolution for the school children. It is about \$4 million per year in the future for the schools, so next year's check should be even bigger than this year's check. This whole matter was brought to our attention by some private attorneys—one is here today, John Bloomquist. We appreciate them bringing this to our attention and the thought they put into this issue very early on in the process involving other litigation.

A vote was taken on the motion to approve. Motion carried unanimously.

Governor Schweitzer said we have several timber sales and I would suggest we take the Bald Hill timber sale separately. The other five are fire salvage and we could take those ones as a block. Let us start with 1107-9.

1107-9 BALD HILL TIMBER SALE

Ms. Sexton said 1107-9 is not a fire salvage sale. It is southwest of Kalispell in a wildland urban interface. It is 2 million board feet and a modified shelterwood treatment. No permanent roads are required. There was one comment in support of the timber of sale.

Motion was made by Mr. Morrison to approve the Bald Hill timber sale. Seconded by Mr. McGrath. Motion carried unanimously.

1107-10 COOKED MOUNTAIN TIMBER SALE (FIRE SALVAGE)

1107-11 DOUBLE BEAVER TIMBER SALE (FIRE SALVAGE)

1107-12 FOURNIER CREEK TIMBER SALE (FIRE SALVAGE)

1107-13 SEARED GULCH TIMBER SALE (FIRE SALVAGE)

1107-14 TIN CUP TIMBER SALE (FIRE SALVAGE)

Ms. Sexton said we have five timber sales that are fire salvage timber sales. Two of these are from the Chippy Creek Fire in the Plains Unit. They are the Seared Gulch sale which is about 3.4 million board feet and the Cooked Mountain sale which is 3.8 million board feet. The Double Beaver sale, which is 3.1 million is board feet, is from the Jocko Lakes Fire. The Tin Cup sale is a smaller sale and is 381,000 board feet from the Tin Cup Fire. Finally, the Fournier Creek sale from the Black Cat fire which is in a wildland-urban interface. There will also be some hazardous fuel reductions done in conjunction with the fire salvage sales. As we had mentioned previously, there will be more fire salvage sales coming. This is about 64 percent total of what we are proposing for fire timber salvage. The December Land Board meeting will have another 23 percent of the sales, which is another 4.5 million board feet. There will be some sales this

winter and spring, but we are trying to get these sales through so most of the harvesting can be done while the ground is frozen in optimal conditions. I want to really thank the staff—I know David Groeschl (DNRC Forest Management Bureau Chief) isn't here because of the moisture in Missoula—but our timber folks have put in a lot of time and effort to get these sales ready for approval and to get them sold. So I really appreciate all of the work by the staff. Just as a tidbit of information, the timber from our salvage sales will be enough timber to build about 1900 homes. That would be the funding for 434 K-12 students, just from the timber salvage sales. This really is a remarkable effort for the forest and a great benefit for the school children of Montana.

Ellen Engstedt-Simpson, Montana Wood Products Association, said this a very good opportunity to publicly thank the Land Board for your approval of timber sales over the past year and your expeditious handling of fire salvage. It is greatly appreciated by our members, and me personally. All of our folks do business in the state of Montana and rely on state timber sales for a solid stable of supply. I'd also like to thank Director Sexton and the fine staff at the DNRC. As she pointed out, they do a yeoman job of doing timber sales as well as taking care of trust lands, along with the Land Board staffers. I appreciate your efforts very much.

Motion was made by Ms. McCulloch to approve the five timber fire salvage sales. Seconded by Mr. Johnson.

Ms. McCulloch said I would like to thank Ms. Sexton and Mr. Groeschl and staff on behalf of K-12 education. When I asked Mr. Groeschl in August why he hadn't brought the salvage sales to us yet, he certainly didn't waste any time getting them to us. So thank you to all of the staff.

A vote was taken on the motion to approve. Motion carried unanimously.

1107-15 DISCLAIMER OF INTEREST – CITY OF BILLINGS

Ms Sexton said this is a disclaimer of interest for the City of Billings. The City of Billings has requested that the state issue a disclaimer of interest for lands which are adjacent to Lake Elmo Drive in Billings to facilitate road reconstruction. There is a possible ambiguity resulting from an earlier Carey Land Act Deed. The department has reviewed the factual allegations and concluded the state has no possible claim to the land, but we request the board's permission to execute the enclosed disclaimer of interest.

Motion was made by Mr. Morrison to approve the disclaimer of interest. Seconded by Mr. Johnson. Motion carried unanimously.

1107-16 RIGHTS-OF-WAY APPLICATIONS

Ms. Sexton said there are several rights-of-way I would like to bring to your attention. First is the Laurel Cemetery road easement. This has been worked on for many years and there have been issues with conflicts with the air space since the airport is nearby. This will provide access to the Veteran's Cemetery and the City of Laurel Cemetery. Another right-of-way I would like to point out is the Marysville Road. This is an interesting one because of a potential claim for an RS 2477. This may have been a pre-existing road before statehood, but that is unclear. So we've taken a rather novel approach, working with the Lewis and Clark County Attorney (Leo Gallagher) because there is a timing issue regarding the approval of the easement for the road. The funding for the easement will be put in escrow pending clarification of whether this is an RS

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2477 road so the county can move forward with construction on the Marysville Road. I'd also like to bring your attention to the Early Springs, LLC. This is for legal access under our new policy, under which a one percent conveyance fee will be included. There is also a bridge easement from the Department of Transportation in Broadwater County. Finally, is the Veteran's Cemetery itself. In addition to the access easement, there is the issue of the cemetery itself.

Motion was made by Mr. Morrison to approve the rights-of-way. Seconded by Ms. McCulloch.

Mr. Morrison said Commissioner Bill Kennedy had intended to be here but was unable to due to health issues, and asked me to make a few points. I'd like to begin by thanking Commissioner Kennedy for his hard work on this. It's taken a long time and he's put a lot of personal time into it. I'd also like to thank Jeff Bollman of the DNRC in Billings who spearheaded this project, and Dave Van Nice of my office who worked with him to bring this to fruition. A couple of points: seventeen and a half percent of veterans in the state of Montana live in Yellowstone County. We are working in conjunction with the United Veterans Council in Yellowstone County to make this happen. There has been legislative approval to build the county cemetery. During the 2007 regular session, the legislature gave approval to extend mill levy dollars for the Veteran's Cemetery. Voters of Yellowstone County overwhelmingly voted to pass a \$1 million levy to support Yellowstone County veterans. Yellowstone County has contracted with the Peaks to Plains Engineering Company, and funding from the first year of the mill levy will pay for the state and city of Laurel leases. There is an aggressive schedule planned including groundbreaking on Memorial Day of 2008, with Phase 1 to be completed by Veterans Day of 2008. The veterans in Yellowstone County are certainly deserving of this. There is widespread popular support, and it is a good thing the Land Board has an opportunity to do here today. Thanks to everyone that I named and any others who helped out.

A vote was taken on the motion to approve. Motion carried unanimously.

1107-17 EASEMENT – LOCKWOOD SCHOOL RELOCATION AGREEMENT

Ms. Sexton said this easement is for the Lockwood School District. They are currently expanding their facility, which would impact some current access on trust lands. So we would relinquish the current right-of-way location and the school district and Yellowstone County would issue a new location of right-of-way access to state trust lands.

Motion was made by Mr. Johnson to approve the Lockwood School relocation agreement. Seconded by Mr. McGrath. Motion carried unanimously.

INFORMATIONAL ITEMS

Governor Schweitzer said he noted that on, November 3rd of this year, Mr. Johnson, commented in the Billings Gazette that he and the Governor fundamentally disagree on how to develop Otter Creek. Governor Schweitzer said he attempted to find out what the disagreement might be and spent time looking at all the minutes and tried out what disagreements there might be relative to developing Otter Creek. He thought the Land Board would be a great opportunity to address this because ninety-nine percent of all the votes the Land Board have, like today, have been unanimous

Mr. Johnson said the fundamental disagreement that he is referring to is the fact that on several occasions the Governor has expressed reticence to move forward with lease sales because of

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entering into what he calls "bargain basement sale prices". We put minimum bids on things we sell all of the time, and in fact we can protect the trust from fire sale prices on those leases. One of the ideas is actually not new, it is in a document we have from Governor Martz's administration where the recommendation is made that the state take the lead on all of the environmental assessments, permitting, and citing so that we can in fact provide some reasonable level of assurance that development would be forthcoming, if someone were to in fact meet the minimum bid price. It is just a different approach, that is all.

Governor Schweitzer said approximately one year ago Mr. Johnson said he was going to send us a letter requesting information on Otter Creek. That was in June of 2006. So we had staff prepare where we were at that time and included Chuck Kerr from Great Northern Properties, the largest coal owner in America, with whom we are in a contractual agreement to co-develop our resources in Otter Creek. We made that presentation at the July 2007 meeting during which Mr. Johnson was absent. Just to get the ball rolling, does Mr. Johnson have an idea what would be a minimum bid or how we would precede forward based on the information provided to Mr. Johnson's staff by the DNRC during the course of the last 18 months?

Mr. Johnson said he was not aware that Governor Schweitzer was going to raise this topic of discussion today. He certainly would be happy to bring hard numbers to the Governor in the near term.

Governor Schweitzer said during the next Land Board could Mr. Johnson make a presentation as to his ideas on the development of Otter Creek?

Mr. Johnson said yes.

Governor Schweitzer said then we will put that on the agenda for December. Just for the record, we have a fiduciary responsibility to the people of Montana to get fair market value on every lease and sale. That also applies to oil and gas leases as well as buying and selling land. He did not think that anyone on this Land Board would suggest that we would sell any of our assets at less than fair market value. Otter Creek is a little bit more complicated to develop a strategy, in particular because there has already been a contract drawn up with one of our co-developers (Great Northern Properties). In July of 2006 when Chuck Kerr made his presentation he cautioned the Land Board on many concerns he had on us moving ahead so that we did get fair market value. His biggest concern was the DNRC and Great Northern trying to sell these assets before there was an infrastructure in place. Great Northern is in the business of trying to sell their coal assets because they are coal developers as well. Naturally the Land Board will take into consideration their ideas, and we also look forward to hearing your ideas.

Mr. Johnson said he would just like to say that he has been as true to his fiduciary responsibilities as anyone on this board.

Governor Schweitzer said this discussion started by giving Mr. Johnson an opportunity to describe his fundamental disagreement in developing the Otter Creek tracts. We've had roughly 36 months for Mr. Johnson to bring ideas forward to the board. Beyond Mr. Johnson doing that individually, each of us has staff that meet monthly with the DNRC. Nowhere in the record has Mr. Johnson's staff brought ideas that are fundamentally different from the rest of the Board. We appreciate Mr. Johnson's active interest in Otter Creek, but we are also interested in his ideas if he has fundamental differences with the Board as he has described to the press. We are not accusing anybody of trying to sell for more or less. And as I've said, ninety-nine

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percent of votes we have with the Board are unanimous, as they were today. It does stand in stark contrast when any member of the board suggests that he or she has fundamental differences with some other member of the board.

Mr. Johnson said I appreciate the opportunity and I look forward to finally providing a detailed presentation at the next meeting for the Board.

Governor Schweitzer said in June of 2006 Mr. Johnson raised this issue and asked for a presentation from the Land Board. We spent about two hours at the July 2006 meeting describing not just Otter Creek, but all of the coal resources, the plans that were moving forward, and the work and the analysis that had been done. Four of the members of the board were here at that time, but we didn't hear any response from Mr. Johnson or any member of his staff after that presentation, so it caught some of us by surprise that he has a fundamental difference from the rest of us. The December meeting will allow you to clarify your position and clear up any misunderstandings.

Mr. Johnson said yes, thank you.

1107-18 PRESENTATION OF FY 2007 HIGHLIGHTS BY TOM SCHULTZ

Governor Schweitzer said we have fiscal year 2007 highlights from Tom Schultz.

Tom Schultz, DNRC Trust Land Administrator, said the intent of this presentation is to provide an overview of the previous year's activities. Director Sexton made a comment about all of the work done on the timber sales. The work doesn't begin or end there. We have about 130 employees on staff who work across the state. We talked about volume of timber. For about every million board feet of timber, that represents one FTE of work. That is not including just foresters, it is hydrologists, wildlife biologists, planners, economists, and other staff that help deal with those issues. We have about 10,000 agriculture and grazing leases across the state. We do an evaluation of those leases about once every ten years, so every year we go out in the field and evaluate about 1000 leases. Every lease evaluation represents about 500 person days in the field. We take a lot of pride in the training and development of the staff that we have and the competence that they provide on the landscape.

One of the things we always talk about is mission. If you do not have a clear mission or vision of where you are going, it leads to confusion and non-productivity within the division. We have a mission that aligns very clearly with the goals of the DNRC and state government as a whole. The first thing is leadership. We really pride ourselves on developing leaders. If we don't have qualified staff that can make good decisions and are competent and work well with lessees on the landscape, then it is impossible to meet Trust Land's mission. I'd like to stress that we try to reach out to different groups to help provide us with leadership skills. At the Regents meeting on Friday, I spoke with President Joe MacDonald of the Salish-Kootenai College. Mr. MacDonald was an individual who we brought to a training session we had about a year and a half ago. He provided his own area of expertise and provided his own thoughts on leadership and how involved he's been at the college up there. He had a tremendous vision of where he wanted to go and brought the college with him, so we try to bring in folks like Mr. MacDonald to help us think about where we want to go.

The three components that make up the Trust Land Management Division mission are leadership, fiduciary responsibility, and stewardship. One of the things mentioned earlier today

was fiduciary responsibility. We have a mandate to generate legitimate, reasonable revenue. You won't hear me use the word "maximize" because that means you look at one thing in isolation of everything else. We pride ourselves on trying to clearly look at the revenue stream, but also balancing the needs of the resource while taking a lot of public input in the process. Finally, I'd like to mention stewardship. We take pride in the fact that we manage these lands in the long term. We don't want to see the resource depleted or the lands disposed of inadvertently and we take a lot of pride in the stewardship that we provide on the landscape.

Here are basic highlights in terms of revenue activity. We get this information every year from OPI in terms of the number of school children that are in the schools. We had just under 150,000 children in the schools, which is roughly 15 percent of the population of Montana. That state share is just under \$4700 per year. If we look at the revenue generated by trust lands it is about 7.25 percent, or \$48 million. In the past we've generated about ten percent, so two things have happened in the past year. One, there has been more money provided for K -12 education, so if our base remains the same, the percentage provided becomes a smaller percentage of the overall funding. Also, this past year we've seen a little bit of a dip in the oil and gas revenues. But still we are typically in the range of seven percent to ten percent of the funding for K -12 education. That equates to just under \$400 per pupil. Additionally, I'd like to mention the technology acquisition fund. These are revenues that are generated from the sale of timber. The K -12 budget is appropriated by the legislature, so whether we contribute five percent or fifty percent, K-12 is still going to get a number that is appropriated by the legislature. The technology acquisition fund money is in effect gravy. It is money that is received in addition to the legislative funding. Timber sale revenue and timber sale volume harvested for common schools was down this year, but it was just under \$900,000.

These are the revenues by trust. We've seen a lot of interest in the past year from the university system in terms of looking at their revenues on the university system lands. So we try to break this out by each different beneficiary. The land board has a trustee responsibility for all of the different trusts, but the primary responsibility at times is common schools because it is 90 percent of the land base. We generated distributable revenues just under \$55,000,000 this year. Distributable revenues come primarily from activities such as timber sales, agriculture and grazing leases, even mineral leases. Those are the resources that are renewable resources. It is the non-renewable resources that are considered non-distributable revenues. If we have royalty payments from oil and gas, from coal, from permanent disposition of easements, or if we were to be selling the land not under the land banking authorities, that would be a non-distributable revenue. Most of the revenues that we generate are clearly distributable. Those go to fund different institutions and they are used in different ways by the different institutions. You can see we have two new trusts this year. The Montana Developmental Center and the Montana State Hospital each had over \$1000. The Land Board accepted a donation from the estate Mr. Sirr. In his will he donated about 2500 acres of grazing land to the state of Montana and he identified three trusts—one was the School for the Deaf and the Blind and the others were the two new trusts.

Agriculture and Grazing Bureau:

- We have four primary programs within the division. The one that manages the most land is the Agriculture and Grazing Bureau. We had agriculture revenues this year just under \$10 million. We had just under \$3 million from farm payments. These agriculture lands represent just under 600,000 acres. Wheat and barley are the two primary products grown. We have about 13,000 acres of irrigated lands. When you look at the

revenue stream from agriculture, we typically average around \$12 or \$13 per acre net on dryland. If it is irrigated, \$27 to \$30 per acre. If it is CRP land, of which we have about 140,000 acres, it is closer to \$30 per acre. Between irrigated and dryland you are looking at doubling your revenue. When you look at agriculture versus grazing, grazing is about \$1.25 an acre net. We have just under 490,000 acres of grazing land and about 600,000 acres of agricultural land. When you look at the agriculture acres, only 13,000 are irrigated. So when you look at the breakdowns, they are what really drive the revenue stream. The grazing revenue this year was just under \$8 million with 1.1 million AUMs. The AUM rate in 2007 was actually up from the minimum of the previous year at \$7.80 per AUM, and that is largely tied to the price of beef. There is a multiplier we have which is just over seven times the price of beef and that gives us the minimum AUM rate for the year. Ninety-three percent of our leases are at the minimum, so that is what drives what happens. For instance, if the AUM rate is up or down one dollar, it is worth about \$1 million across the state. So any effect—whether it is tied to the Land Board either reducing the multiplier or the price of beef—can have a million dollar impact by one point up or down.

- Stewardship is another important activity. In 2007 we inspected about 903 leases. That was over 1400 tracts. We have an archaeologist on staff that looks at tracts that are being sold or have activities on them. We also have paleontological surveys. In the past we've actually found a triceratops on state land. There have even been T-rex remnants partially found on state land. So pretty much anything you can imagine happening across the landscape, we do it on trust lands. We have done willow collections and planting on the Big Hole and some grayling restoration with FWP. One of the things we are most proud of is the weed control with biocontrol agents. A lot of the biocontrol work done in Montana was actually started by Craig Roberts who was a DNRC manager out of Lewistown (retired). He got the ball rolling, and every year we go out and collect spurge beetles and biocontrol agents across the state and distribute them across trust lands to reduce the weed populations. We've also worked to clarify water rights on state land during the past year. Another thing we've looked at is identifying high hazard dams where lessees have over time put in dams, whether for irrigation purposes or stock watering. We are trying to make sure we've reduced the hazards on those dams.
- A little bit about crop production—if you look at the acres of production you can see the actual quantity of production over the past four years. So you can see production in 2007 was slightly down, but rentals were up. If production is down but rentals are up that means the prices were up for commodities. Production year to date in 2008 is about half of 2007, yet the rentals received this year are equal to 80 percent of all rentals received last year, so commodity prices are even higher in 2008. You may have even heard that wheat has been going for \$12 per bushel. Revenues in 2007 were up because even though production was down, prices were up for both wheat and barley.

Forest Management Bureau:

- In the past year we've sold 53.3 million board feet. The land board approved 25 timber sales last year which was just over 50 million board feet. We also had 44 timber sale permits for just under 3 million board feet. A timber sale permit is for a very small volume. An individual logger might be out there looking for work and he could see a small area with some timber blowdown or beetle infestation. He will identify that, call the

department, and we'll try to put up a permit to harvest that volume. One of the big differences between this year and last year is the volume harvested. It's not what we sell, it's what we harvest. Timber sale contracts are typically three years in length and can actually be extended out to five years. The volume harvested last year was 32 million board feet, and that is a reflection of price. So it is no different than any other section of the economy. The purchasers of timber sales are looking at harvesting volume when prices are high. They purchase at a high price, but prices dropped so they are not harvesting it as quickly and the volume is down.

- We expect to have the draft EIS for the Habitat Conservation Plan completed sometime in the next six months and out for public review. It is something we have been working on for many years. The HCP is for us to work with the Fish and Wildlife Service and FWP to identification conservation strategies for the threatened and endangered species in Montana in order to give us greater certainty that what we are doing with our forest management isn't going to hurt the species. At the same time it gives us protection from lawsuits because the Fish and Wildlife Service is supporting what we are doing. Additionally, we also inventoried 25,000 acres of our forested lands just to get better data.
- As you can see on this slide, in the last eight years there was a lot of fluctuation between volume of timber sold and volume harvested. In 2005 the two were roughly equal, as they were last year. Last year we had a lot of salvage timber sales from the previous fire season. This year the volume harvested was down from the volume sold.
- When you look at revenues it's a function of two things—price and production. I just talked about production. A trade organization puts out the price of lumber quarterly. There is a correlation between the price of lumber and what you get paid for your standing trees or stumpage. The gap has closed since 1980, but that random lengths number is not a state number, it is a regional number. You can see that the price of lumber went down in 2007, and so did our stumpage price. The interesting thing to note is the drop in lumber prices between 2005 and 2007—it was greater in 2007 than in 2005. Yet we are still receiving the same price for stumpage as we did in 2005 so there was a greater drop in lumber prices, so stumpage prices dropped, but not as much as they potentially could have. The average price for 1000 board feet is just under \$250 for timber sold on state lands in 2007.
- One of the things we have talked a lot about is access. The Land Board adopted a new access policy last year. What we really want to make sure we are communicating to the Land Board and other folks is that the acres that we both grant and receive are equal. So you can see we accessed nearly 10,000 acres trust lands. The public access was even greater because we had received other grants for nearly 12,000 acres. So for the last three years we've been looking at this number. Last year we were under 4000 acres, the previous year we were at 8000 acres, and this year we're at 12,000 acres. Incrementally, we are trying to perfect permanent access, not just for management purposes, but also for the public. We talk about reciprocal a lot—what we receive compared to what we grant. We received in terms of mileage just under 24 miles of access and we granted about 18 miles.
- Some current restoration activities on trust lands are reclaiming old roads which we typically do on timber sales. We look at BMPs—replacing culverts, relocating roads,

stabilizing roads, putting in new culverts. We also completed the riparian fencing and fish habitat on the Sula South Project on the timber sales we had after the Sula fire. We also planted 550,000 seedlings at Sula over the last two years. We take stewardship very seriously.

Minerals Management Bureau:

- A big reason for the drop in revenue in 2007 is a drop in bonus bid revenue. You can see revenues were about \$30.5 million. Most of that does come from oil and gas while almost \$4 million were from coal. That was about a \$12 million drop over the last year. Here are the gross revenues for the last several years. Oil and gas makes up about 90 percent and coal about 12 percent of the revenues. Even though we were down in 2007 from 2006, we are still up substantially in the long-term average, even going back to 2000. I also mentioned that revenue is a function of both price and production. The average price per barrel that we received was \$55.85. We have been hearing forecasts of oil for 2008 going up to \$100 per barrel. \$55.85 is what we received in Montana: \$100 is a West Texas number. We had just over five and a half million barrels of oil produced on state lands this last year. The revenue number in 2007 is actually higher than 2006—what we saw was actually a reduction in bonus payments. Gas revenue is also a function of price and production. Gas prices were down a little \$5.13 per mcf—as was production. On average we are generating about \$80,000 per month with coal bed methane on state wells. Monthly production has dipped over the last year. The royalty payments have gone down a little, but it's not a huge swing from last year. We are up from three years ago, but down from two years ago.

Real Estate Management Bureau:

- In 2006 we kicked up sales from land banking so we made nearly \$11 million and that includes interest earned from land sales. We made over \$1.3 million from residential leases which are primarily cabinsite and homesite. Easements were about \$6.5 million. We had a big easement up in Kalispell on Section 36—the Department of Transportation paid us for the Highway 93 bypass. We have just under \$100,000 in revenue from conservation easements and licenses and about \$1 million in commercial leases.

Auditor Morrison said I don't know how the accounting rules work here but I assume there is some different treatment for revenue that comes from land banking sales because it is not really like normal income to the trust—it is sequestered for specifically for land banking.

Mr. Schultz said the interest earned off of that money actually goes in the permanent fund for that statute, but the proceeds sit in the land bank fund and are reinvested in land, so you'll see that both as a revenue and an expenditure. It nets out for the most part.

- A big part of the land banking program is to diversify the holdings, increase revenue, and increase public access. These are the lands we sold via land banking. It was just over 19,000 acres and generated about \$10.6 million. The overall weighted average returned from the land we sold was about 0.8 percent. One of our tasks in land banking is to acquire land to generate equal or greater revenue in addition to increasing public access. Just under 19,000 acres of the 19,000 acres we disposed of had no public access.

- We sold 19,000 acres and acquired 24,300 acres. We spent \$9.998 million, so we actually acquired more acres and spent less money than we took in. The appraised value was \$10.1 million, so we actually paid less than appraised value for all the properties we bought. You can see the annual income stream and the estimated rate of return was about 1.7 on the lands we acquired. We doubled our overall return. We increased public access by 24,000 acres, paid less than what the lands appraised for, and we tried to buy in the counties in which we sold—though that did not happen in all cases. In Custer County we bought 18,000 acres from the Tongue River Ranch and sold 9500 acres. We really tried to meet the intent of the of the statute and worked with the staff and the public during the last year. Another part that we talked about are the commercial properties. Glacier High School opened last year in Kalispell. Also, Costco, Lowe's, Starbucks, Holiday Inn Express, and Dave's Barbeque opened as well. They are looking at opening a McDonald's, too. Next time you're up in Kalispell by the DNRC office, all of the commercial properties in the area fall under this section. We are currently generating from that section close to \$500,000 per year. That used to be an agricultural parcel that generated \$3000 per year and those rentals will continue to go up with appraisal prices. The Forest Service will also lease on the section with the DNRC office, so we hope to better serve the public by being in a centralized location. As I previously mentioned, we had a permanent easement for \$5.7 million dollars for the Kalispell bypass.
- Finally, there has been a lot of discussion about wind energy. DNRC makes up 13 percent of the turbines on the Judith Gap Wind Farm. We generated about \$50,000 last year from the lease. Prior to that it was grazing land generating \$1.25 per acre. So, a huge turnaround in revenue. We are trying to diversify, but also provide green energy. There are two other areas we are currently working on: Geyser and Martinsdale wind farm production. And again, the state land is not the sole area of the project, but it is a component of the project.

Staff Awards:

I talk a lot about staff and the exceptional work they do. From the Agriculture and Grazing Bureau, Dave Mousel was Land Use Specialist of the Year and Stephanie Kellogg got the Staff Support Award. Chris Pileksi out of our Eastern Land Office in Miles City did a great job putting up timber salvage sales last year and is Forester of the Year. Bob Sandman has been a key leader at our Northwest Land Office and has received the Division Administrator's Award.

Mr. Morrison said I'd like to thank Mr. Schultz and his staff. You do great work.

PRESENTATION OF 2007 REVENUE CHECK TO SUPERINTENDENT OF PUBLIC INSTRUCTION

Ms. Sexton said we have with us right now some members of Mr. Wirak's Fourth Grade Class from Jefferson School. Superintendent McCulloch will make the presentation of the checks to the class. The check for the Montana Public Schools is in the amount of \$48,609,316. The check for the Technology Acquisition Fund \$895,841.

Ms. McCulloch presented the 2007 revenue checks.

Governor Schweitzer asked the children to come forward to the podium and announce their names and ages.

Mr. Wirak's Fourth Grade Class introduced themselves to the Land Board.

Governor Schweitzer asked if there was a member of the class who would like to speak before the Land Board.

Michaela Friddle, Jefferson Elementary fourth grader, said I would like to thank the second graders for drawing the background of the check and everyone here.

PUBLIC COMMENT

Ellen Engstedt-Simpson, Montana Wood Products Association, said I am extremely pleased to be able to stand before you and support this year's contribution of nearly \$900,000 into the timber technology account. This is one direct link from the harvest of timber from state trust lands to classrooms filled with Montana school children, like the ones here today. The reason the fund was set up was solely for the rental, purchase, repair, and maintenance of technology equipment such as computers and network access. The sustained yield figure of 53.2 million board feet contributes to Montana's school children and we in the timber community are proud to be part of that contribution. These dollars are not part of the base budget because they are not legislatively appropriated, so this money is gravy to the schools. These funds are also not levied on local tax payers and that is a really good thing too. Out of this account this year, Townsend K-12 has received \$4200, Helena K-12 has received \$46,000, and Missoula K-12 has received \$59,000. So that should purchase a few computers and some other technology for Montana's school kids. Thank you.

Motion was made by Mr. Morrison to adjourn. Seconded by Mr. McGrath.